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Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: *Ex Parte Presentation* in CC Docket No. 96-45
(National Telephone Cooperative Association Petition for Reconsideration and Clarification of Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking in CC Docket No. 96-45, and Report and Order in CC Docket No. 00-256)

Dear Ms. Dortch:

Valor Telecommunications, LLC ("Valor") supports NTCA's proposal to amend the safety valve portion of Rule 54.305 to permit rural carriers purchasing high-cost exchanges to receive Universal Service Fund (USF) support during their first year of operation.[1] The USF was designed to provide support to telecommunications carriers operating high cost rural exchanges and create incentives for investment in rural America.[2] This support was intended to narrow the gap between the services offered to rural customers and those offered to urban customers.[3] The safety valve rule was adopted to ensure that rural carriers purchasing exchanges from larger carriers that were not eligible for significant universal service support, due to the effects of cost averaging across their networks, would receive some universal service funding to maintain and upgrade their new exchanges. In its current form,

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1 NTCA Petition for Reconsideration and Clarification (filed July 5, 2001) ("NTCA Petition").

2 *In the Matter of the Federal-State Joint Board on Universal Service; Muti-Association Group (MAG) Plan for the Regulation of Interstate Services of Non-Price cap Incumbent Local Exchange Carriers and Interexchange Carriers,* Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking in CC Docket No. 96-45, and Report and Order in CC Docket No. 00-256 (May 23, 2001) at ¶¶ 91-120.

3 *Id.*

however, the rule prevents companies from receiving support during the critical first year of operations, because a carrier's "index year" expense adjustment is not calculated until the end of that first year.[4] NTCA's proposed rule change would remedy this gap by allowing carriers to receive safety valve support during the first year of operations, by defining the index year expense adjustment for the first year of safety valve support as the previous owner's expense adjustment during the last calendar year before the sale.[5]

Valor agrees with CenturyTel that expanding the safety valve rule will promote the policy goal of encouraging early investments in network infrastructure during the first year after purchase.[6] In its current form, the rule provides carriers with a perverse incentive to delay making the capital expenditures necessary to improve service quality until after the first calendar year of operations. These delays harm the carrier's customers and the public at large, given that:

- The exchanges subject to the rule have often suffered years of neglect, and require immediate repairs and/or upgrades to enable the provision of modern communications services to consumers;
- Additional expenditures are often required during the first year due to business decisions of the prior owners during the extended closing period between the sale of an exchange and the changeover of control;
- State regulatory commissions often impose immediate upgrade and repair requirements as a condition of the purchase; and
- The first year that a carrier operates an exchange is the year that most of its customers will form a lasting impression of the quality of its services. Failure to improve the network immediately may irrevocably damage the carrier's relationship with its customers.

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4 The safety valve rule allows carriers to receive support for fifty percent (50%) of the positive difference between their expense adjustments for "subsequent years" and an "index year." 47 C.F.R. § 54.305(c) (2001).

5 NTCA Petition at 6.

6 Comments of CenturyTel, Inc. (filed July 31, 2001).

Valor's own situation is a case in point. Valor was formed through the purchase of approximately 550,000 rural lines from GTE in Arkansas, Texas, Oklahoma, and New Mexico. As is typical with many large incumbent LECs, GTE focused most of its investment in its exchanges in large urban areas, allowing its smaller exchanges to fall into disrepair and keeping its rural customers from receiving high quality service. This problem was exacerbated by the one-year period between the sale of the exchanges and the changeover of operational control, since GTE had limited incentive to invest in the lines during the one-year window between the sale and changeover of operations. Thus, Valor acquired a network that was in need of both immediate upgrade and maintenance. The NTCA's proposed rule change provides a necessary incentive for companies like Valor to invest in these expensive networks. If Valor or others purchase similar high cost properties in the future, it is important that this incentive be in place to facilitate sufficient investment in the acquired exchanges.

As NTCA points out in its proposal, numerous checks within Section 54.305 and in the marketplace will ensure that abuses of the safety valve rule do not take place even if support is provided in the first year. First, the carrier is only reimbursed for half of the difference between the first year expense adjustment and the index year expense adjustment. Second, safety valve funding is capped at five percent (5%) of USF funding in each calendar year. Third, carriers are overseen by state regulatory agencies. Fourth, competition with wireless and other carriers will discourage unwise or extravagant investments.[7] Thus, AT&T and WorldCom's arguments that the proposed rule change would encourage rural carriers to make reckless and unwise investments and drive up the market prices of rural exchanges are wholly without merit.[8]

AT&T also claims that NTCA's proposal is impractical because non-rural LECs report their expenses by study area rather than by the individual exchange. As a result, they assert that there is no accurate data available as to the actual expenses incurred by the incumbent LEC for each of the individual exchanges it sells.[9] However, the average per line loop cost of an ILEC within a particular study area is readily available and could easily be used to estimate the index year expenses per

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[7] NTCA Petition at 7-8.

[8] Opposition to Petition for Reconsideration of AT&T (filed July 31, 2001) at 2-4; Opposition to Petition for Reconsideration of WorldCom (filed July 31, 2001) at 3 .

[9] Opposition to Petition for Reconsideration of AT&T (filed July 31, 2001) at 4.

line for a purchased exchange. This figure averages the expenses across both high and low cost lines within a given study area and would thus provide a conservative figure for the calculation of first year USF support under the proposed rule change. Other relatively simple methods of determining the expenses of a given exchange also exist. Thus, AT&T's unfounded accounting concerns should not preclude the Commission from implementing the proposed rule change.

Furthermore, the proposed rule change would not seriously deplete the funds available for safety valve support. According to a recent Legg Mason study, if no additional lines are sold between now and 2005, rural carriers could receive as little as ten percent (10%) of the available safety valve funds.[10] Even assuming that an additional one million lines are sold annually between 2003 and 2005, carriers could receive less than twenty-five percent (25%) of the available safety valve funds.[11] The results of the study underscore the need to include first year investment in safety valve support if the mechanism is to meet its intended goals.

The USF was designed to assist high cost rural carriers in providing their customers with access to telecommunications services comparable to those enjoyed by individuals in urban areas.[12] All of the investments made by Valor during the first and subsequent years that it has operated its exchanges have been made in pursuit of

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10 *Universal Service Rural Task Force Order, Implications for M&A*, Michael J. Balhoff, CFA, Managing Director, Legg Mason (presented June 19, 2001) at 7.

11 *Id.*

12 47 U.S.C. § 254(b)(3) (1996).

this goal. The Commission should approve the rule change proposed by NTCA so that rural carriers such as Valor can continue to improve the quality and reliability of the services that they provide to the millions of Americans living in rural areas.

Respectfully submitted,

Gregory J. Vogt

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